The power of pricing

How to make an impact on the bottom line

60%

Nearly 60% of survey respondents said that their pricing approach included simple rules such as cost mark-up or matching competitors

40%

More than 40% of survey respondents rank 'more effective price structuring' as their first or second choice strategy for increasing profitability

25%

25% of survey respondents have little or no understanding of what their customers value

5%

Less than 5% of survey respondents score in the top quartile on all four aspects of pricing

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Contents

Introduction 1

About this report 2

Pricing for growth 8

How do companies approach pricing?..................10

What are the leading companies doing? 16

The four aspects of pricing................................ 24

Conclusions and key takeaways 34

Want to find out more? 36

Appendix: Home countries of respondents.......... 37

Introduction

David Lancefield

In a volatile and competitive market, it is more important than ever to give pricing the attention it deserves. Even small improvements can significantly improve the bottom line, with a 1% price increase typically delivering an 11% impact on profit. And used poorly, it can result in a loss of customers and a backlash from important stakeholders.

We asked pricing specialists from over 500 companies around the world about how they approach pricing. The results show significant trends in pricing capabilities and practices between different industries and countries, and highlight a number of opportunities for further improvement.

Our research shows that although pricing issues vary, there is a common interest in pricing strategy and its potential to help achieve growth.

We found that:

- More than 40% of respondents rank 'more effective price structuring' as their first or second choice strategy for increasing profitability
- A further 17% believe that price pressures will lead to falling margins

But...

- Nearly 60% of respondents' approach to pricing relies on simple rules such as cost mark-up or matching competitors
- 25% of respondents have little or no understanding of what their customers value
- And less than 5% of respondents score in the top quartile on all aspects of pricing.

Whilst pricing has the power to improve the bottom line, it doesn't get the attention it deserves. We hope that our study addresses this by giving you some stimulus, insight and challenge to help you use pricing more effectively. If you feel we can help you make improvements to your pricing, please do get in touch.

David Lancefield
Partner, PwC

"When bosses promise to make their companies more profitable they usually say they will do so by increasing sales or cutting costs. But a third road to profits is rarely mentioned: putting prices up."

The Economist, July 2013

About this report

Welcome to our first global pricing report. We've surveyed over 500 companies from around the world to get insight into how they approach pricing.

We think companies who are getting pricing right are able to tap into significant revenue growth opportunities. We tried to identify the proportion of companies that are really 'best in class' and in what areas others may be falling short.

The survey

The survey contained 26 questions focussing on approaches and perceptions of pricing. We also asked respondents for company descriptions (such as industry, size, turnover) to help us understand and identify any trends by type of company. All respondents are anonymous.

Pricing philosophy

We asked respondents how they position pricing within their overall business strategy.

In particular:

- How important is pricing in their growth portfolio?
- How can pricing help improve business performance?
- How best can pricing be used to stimulate growth?

How an organisation answers these questions affects how it sets and implements its pricing strategy.

Pricing practices:
Pricing can appear to be a complex subject. We believe that looking at the following four aspects can help to simplify pricing decisions you face.

"Pricing is one of the building blocks of marketing that appears to be easy to understand, but is probably one of the most difficult [to get right]."

Business Insider, October 2013

The four aspects of pricing

Industry

- How effectively do you track external factors?
- Do you use this information to set prices?
- Do you consider factors that impact the whole economy (e.g. commodity prices) as well as those specific to your industry (e.g. the pricing strategy of competitors)?

Customer

- To what extent do you identify different groups of customers, understand their preferences and use this information to establish their willingness to pay?
- Do you carry this forward into your pricing strategies?

Transaction

- Do you really understand in detail the profitability of your different products and customers?
- How do you use this to influence pricing and focus sales and growth efforts?

Operations

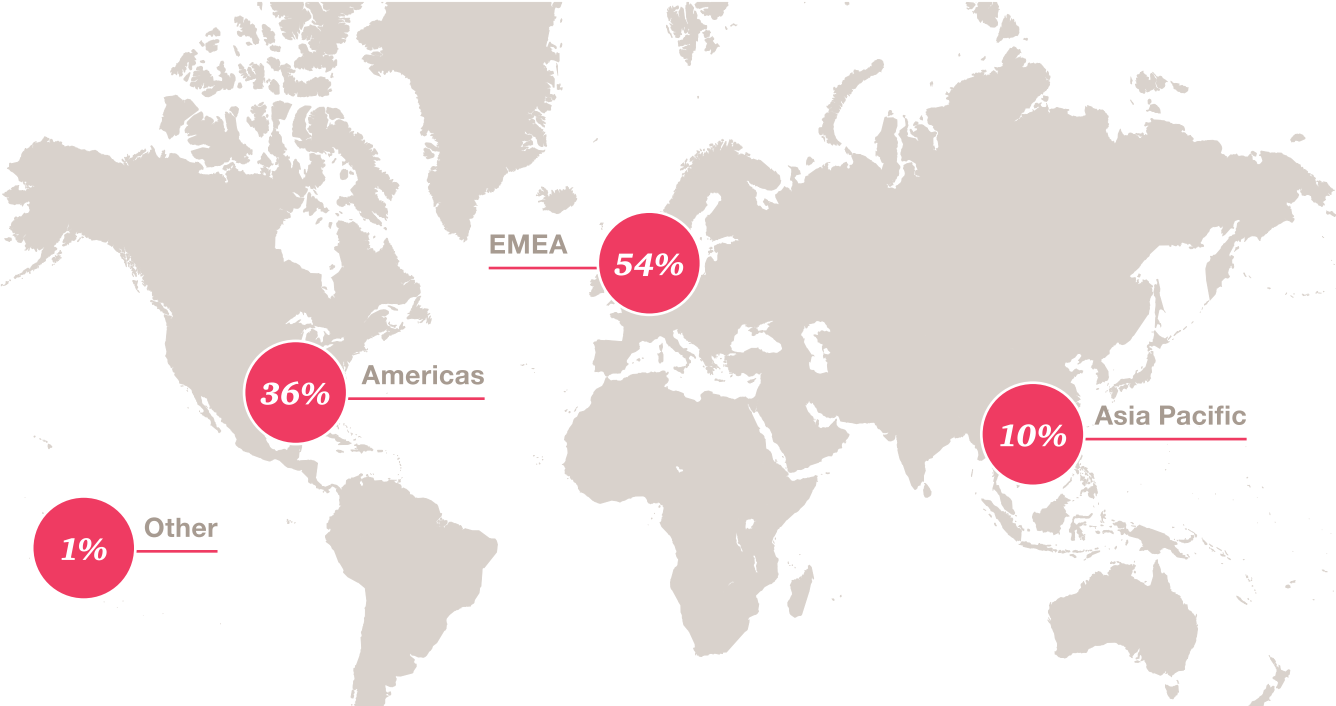
- Do you have in place the necessary structure, systems and processes to properly embed each of the other aspects in your price setting process?
- Are you able to monitor and control pricing across your business?

Who participated?

The survey ran between April and July 2013. In total, individuals from over 500 organisations responded, from over 20 different industries, based in over 40 different countries. The summarised geographical breakdown of responses is shown below in Figure 1.

A full list of countries surveyed is contained in Appendix 1.

Figure 1:
Location of respondents



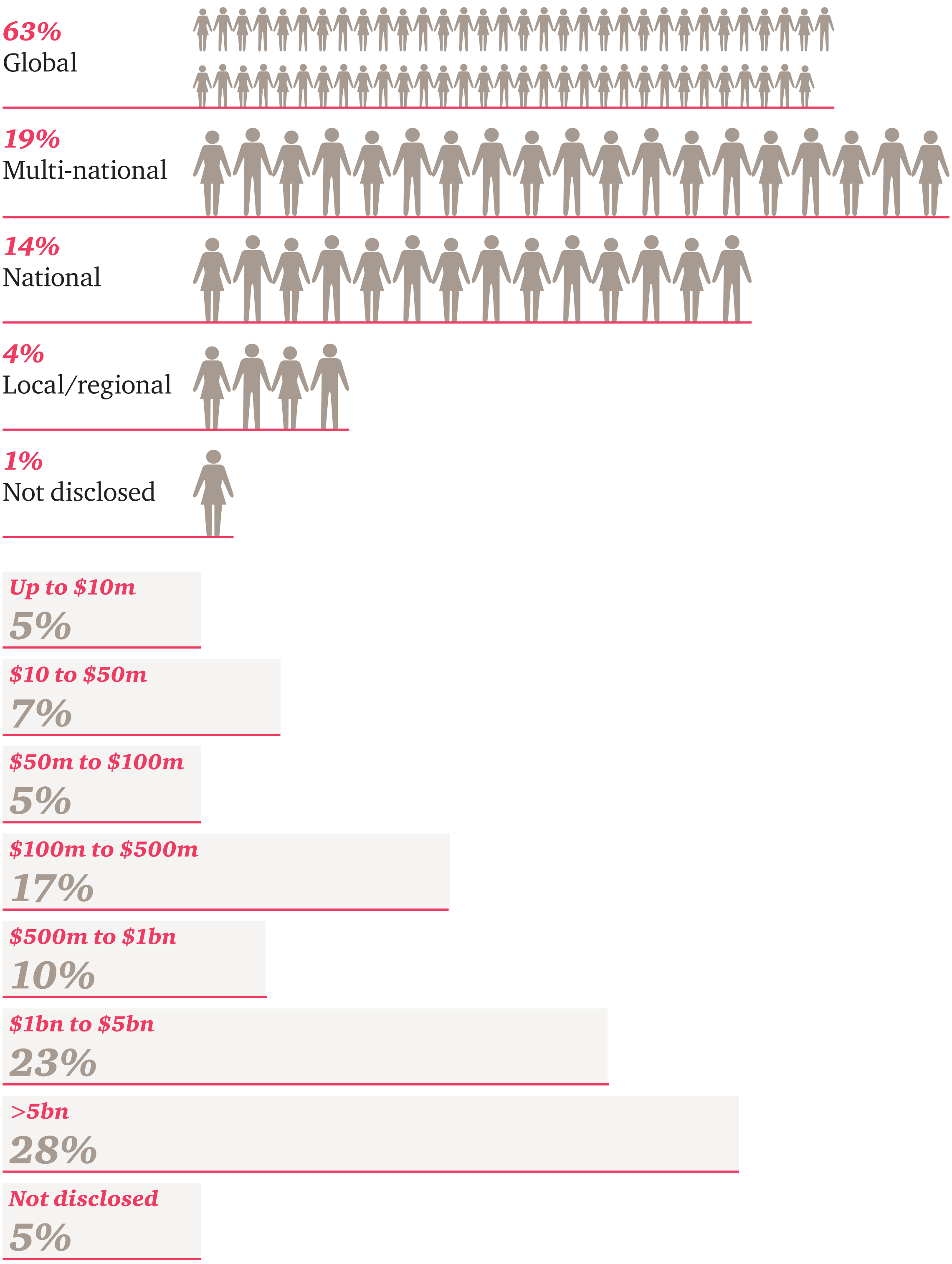
500
Companies responded

>20 Industries covered

Countries responded **>40**

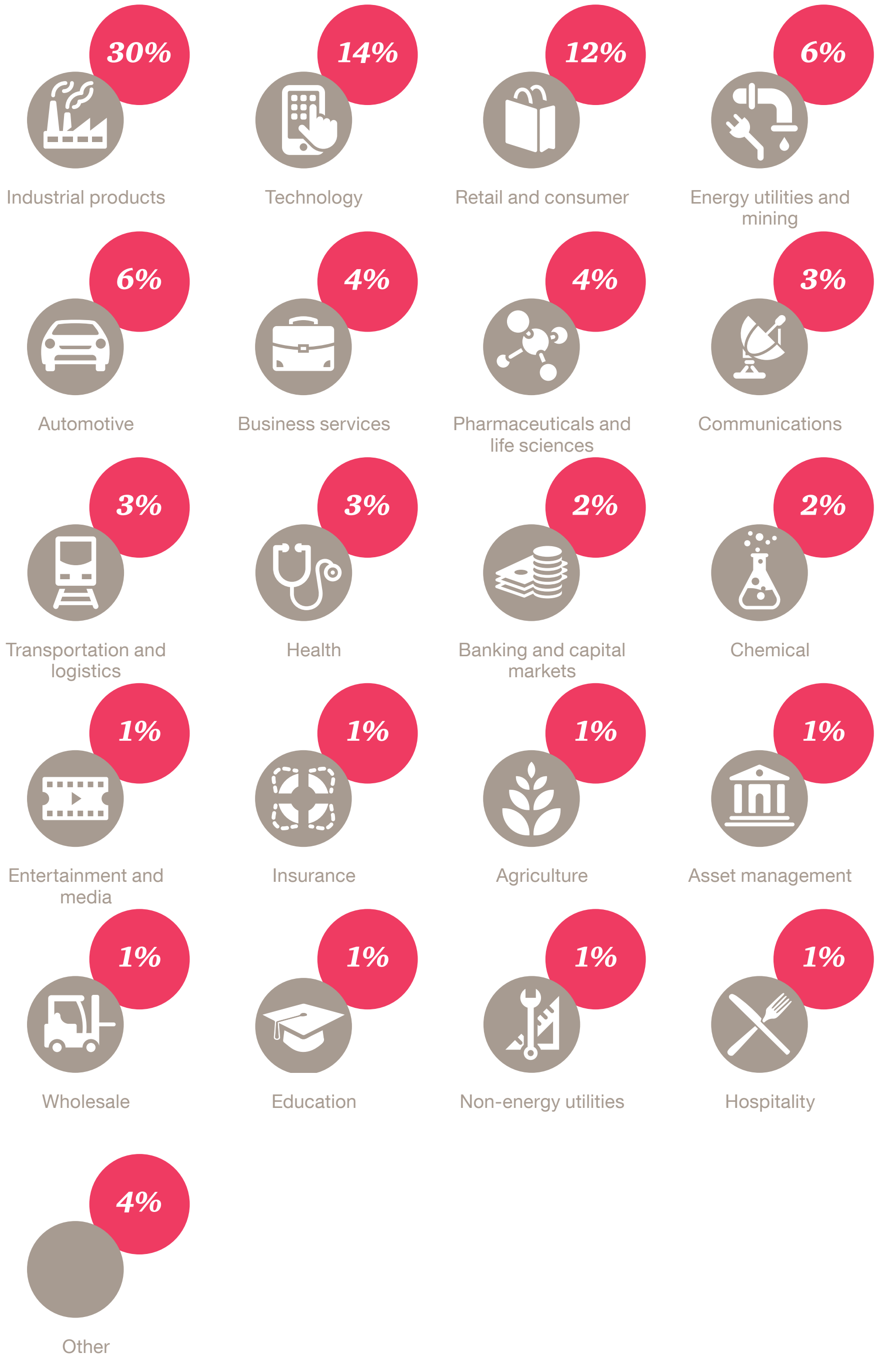
The size of the company also varied between respondents, with more than half representing global companies with revenues in excess of $1bn.

Figure 2:
Reach and size of respondents



The survey attracted responses from companies across a broad range of sectors. This demonstrates that although pricing issues vary, there is a common interest in understanding how they can improve the way they use pricing to deliver profitable growth. The breakdown of responses by sector is shown in Figure 3.

Figure 3:
Breakdown of respondents by sector



Note: *Where we later examine responses to certain questions by sector, we avoid showing results for individual sectors with less than 25 responses (5% of all responses), to ensure conclusions are statistically robust.*

Over half of the respondents listed their job title as Pricing Manager, Pricing Director or CEO.

Pricing for growth

The challenges

Consensus economic forecasts predict a long period of disappointing GDP and consumer spending growth in western economies, lasting into the mid-2010s. We expect there to be periodic bursts of inflation, driven by energy and commodity price movements, adding to growth volatility. Prices for energy and other natural resources are expected to be high and financial market volatility is forecast to continue. Set against this, the prospects for some emerging economies appear far brighter.

Leading companies are using pricing to lift sales growth in spite of tough economic conditions

Starting your growth journey

In light of the above, we believe that some approaches are much more effective than others to navigating your way towards two outcomes:

- Profitable growth now for your business; and
- A better 'growth fitness' that will allow you to identify and capture future growth opportunities more effectively than your competitors.

This survey focuses on pricing, one of the most powerful and effective ways to achieve profitable growth. An increase of 1% in sales volume will typically have a 3% impact on operating profit, since together with the increased revenue there is a corresponding increase in variable costs. Meanwhile a 1% increase in average selling price will typically lead to an improvement of 11%.

Volume growth is hard to achieve and significant cost reduction opportunities have been largely exhausted for some organisations.

Before the financial crisis, a helpful economic climate was conducive to company growth. This is no longer the case. M&A can be very effective in kick-starting growth, but is not without its challenges given prevailing uncertainties.

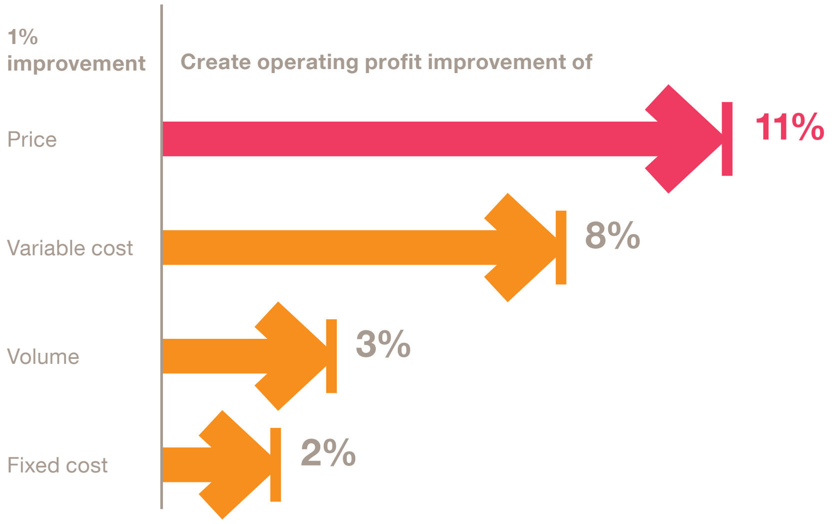
In developed economies, many companies have exhausted significant cost reduction opportunities. And digital technology has made prices more transparent, resulting in greater customer churn - representing both an opportunity and a threat.

All of this means that consumers are placing more importance on the price they pay when making purchasing decisions.

Given this context, it is clear that getting pricing right is critical, especially when it comes to:

- Launching new products and services;
- Responding to competitors changing their pricing;
- Looking to make multi-channel operations more effective;
- Reviewing the profitability of your product portfolio; or
- Responding to considerable churn from your products and services.

Figure 4:
Typical operating profit improvements from different levers (illustrative)



Source: PwC

How do companies approach pricing?

We first wanted to understand perceptions on the role pricing can play in improving profitability.

We asked companies to rank a number of different strategies that could potentially increase profitability. We also asked them what changes they are expecting in net margins over the next three years and what they expect to drive any changes.

17%

17% of respondents believe that price pressures will lead to falling margins.

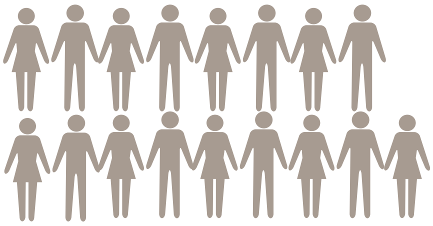
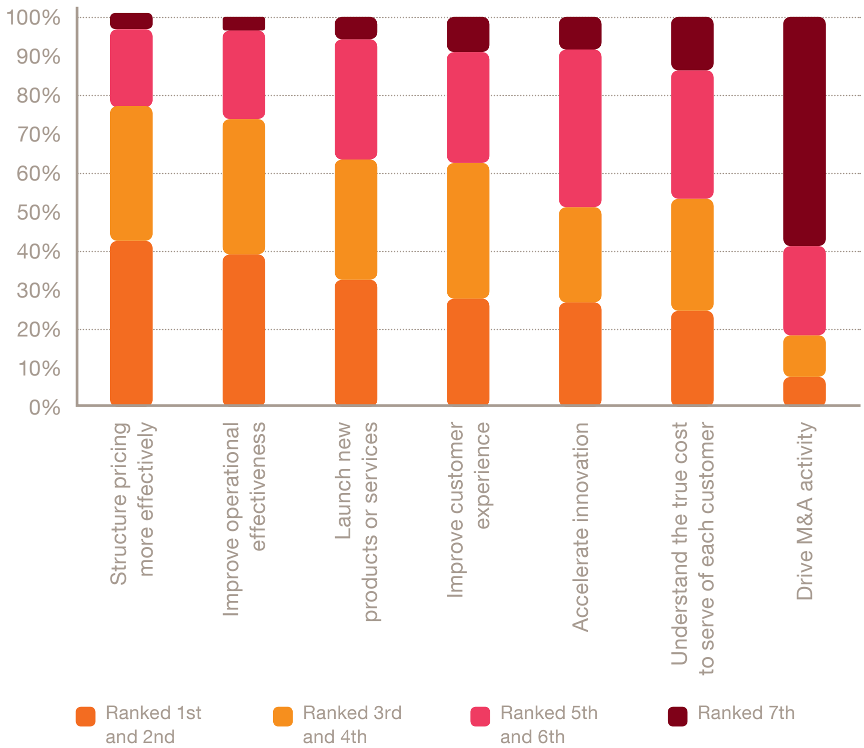


Figure 5:
Ranking of strategies to improve profitability from most effective to least effective



43% of companies ranked more effective pricing as their first or second choice strategy to increase profit margins. Perhaps surprisingly given the support it gives to effective pricing, understanding the true cost to serve was ranked 2nd last.

25% of respondents ranked pricing strategy as the fifth or lower ranking strategy to increase profit margins. It's possible that those who ranked pricing as less effective are those companies who already consider themselves to be relatively sophisticated and therefore are likely to believe they have already exploited the potential effect of pricing.

The responses in Figure 6 are an interesting contrast to Figure 5. Although 43% of companies think better pricing would be the first or second best strategy to grow margins, just 26% actually expect margins to improve over the next 3 years due to price increases. This may suggest that not all respondents expect their companies to execute more effective pricing strategies. Interestingly, of the respondents expecting better margins from price increases, only 43% believe themselves to have a more sophisticated pricing strategy than their competitors (against 41% from the complete sample).

The respondents who expect margins to fall due to falling prices emphasise the importance of a pricing strategy. An expectation of falling prices implies respondents anticipate they will operate in a highly competitive market where it will be necessary to discount to maintain market position. In this environment, effective segmented pricing has greater potential to help protect margins by controlling discounts and identifying other factors that can support a higher price.

Over a quarter of respondents expect margins to stay roughly the same over the next 3 years. This is surprising given the uncertainty and volatility of today's economic climate. However, this could be because many of these companies apply a fixed mark up to costs. Our survey responses also show that of the 141 companies expecting stable margins over the next 3 years, 56% said they set prices by applying a fixed mark-up to costs - compared with 50% of the companies not expecting stable margins.

In Figure 7, almost half of respondents indicated that their company has a formal pricing team in place, reflecting the increasing significance that is being given to effective pricing strategies. This percentage drops slightly (from 49% to 46%) as the size of the organisation grows (revenue over $1m), most likely reflecting the more 'hands-on' approach of senior management in smaller firms.

Figure 6:
Breakdown of expectations of net profit margins over the next 3 years

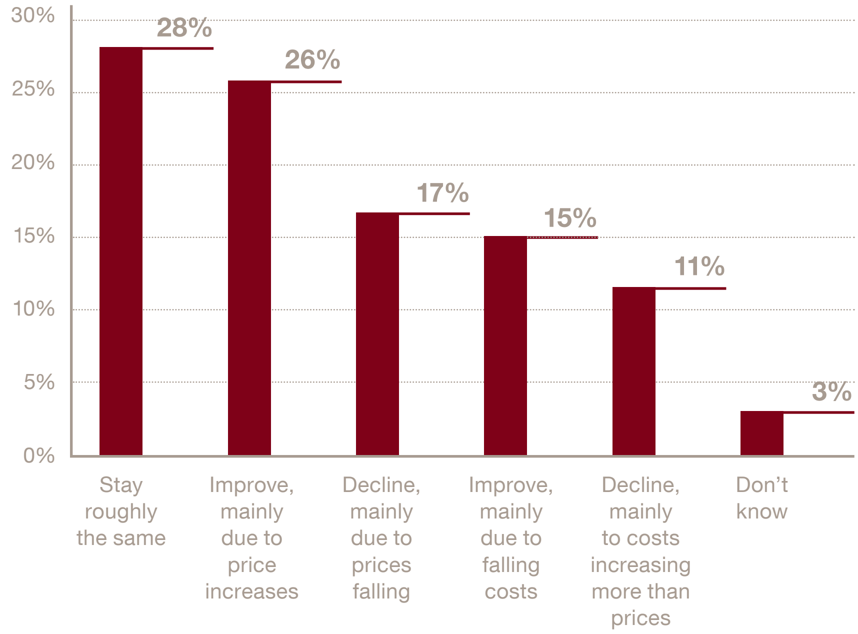
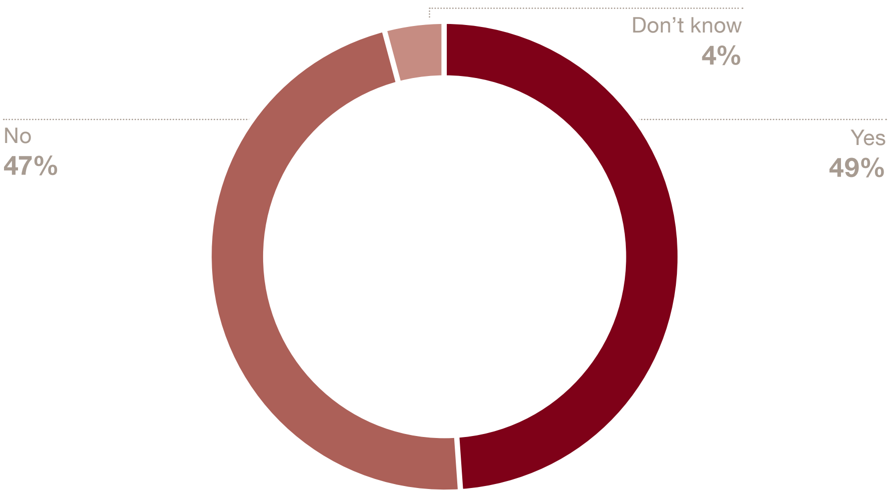


Figure 7:
Breakdown of respondents with pricing board



55% *55% of respondents rarely or never seek external advice on pricing*

Figure 8 shows the percentage of respondents with a pricing team by sector. Over 60% of the technology sector respondents have a pricing team in place. This is significantly higher than the percentages observed in other sectors.

This is perhaps not surprising given that it undergoes vary rapid product innovation with changes in cost and customer willingness to pay, and has therefore been quicker to focus on pricing. At the other extreme, the automotive sector has the highest percentage of companies who said they did not have a pricing team.

Another indicator of the importance companies attach to pricing is given by how often they seek specialist advice.

Achieving pricing excellence is complex. It can begin with a basic review of customer or product profitability. But to achieve pricing excellence there is much more to consider including:

- pricing strategy
- price optimisation
- operating model (people, process & technology)
- change management

Businesses are often not equipped with the necessary skills and expertise to address all of these.

Companies that understand the value and complexity of getting pricing right are more inclined to seek specialist advice.

Figure 8:
Breakdown of respondents with pricing board by sector

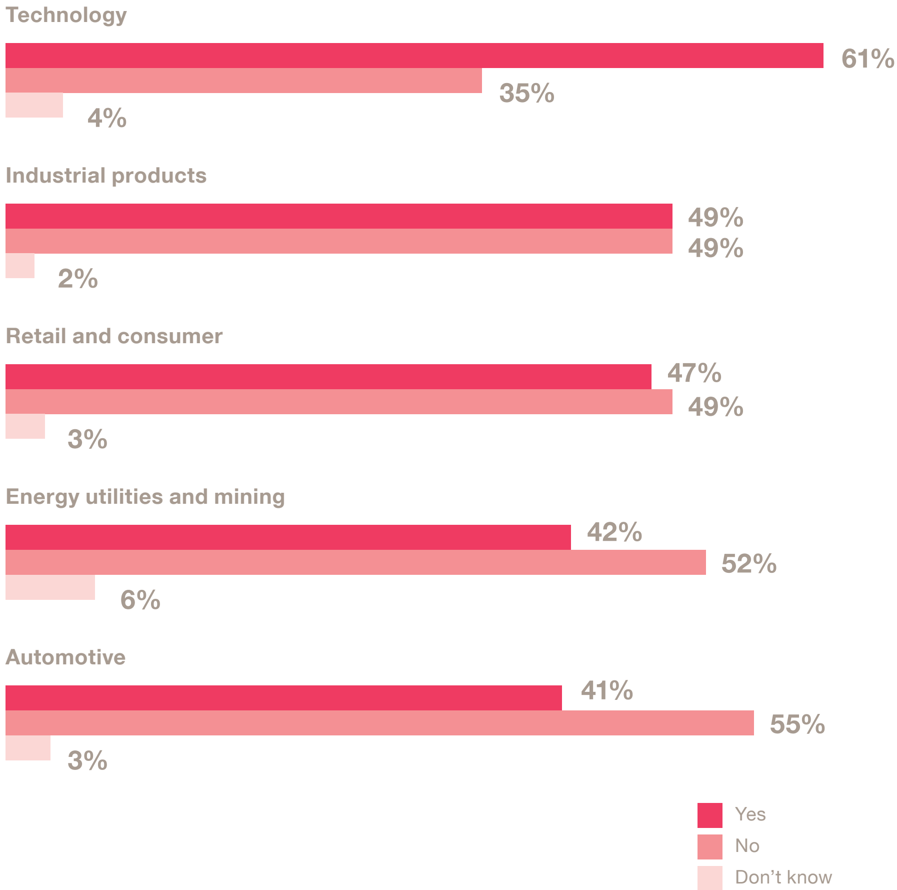


Figure 9:
Breakdown of respondents that seek external advice on pricing

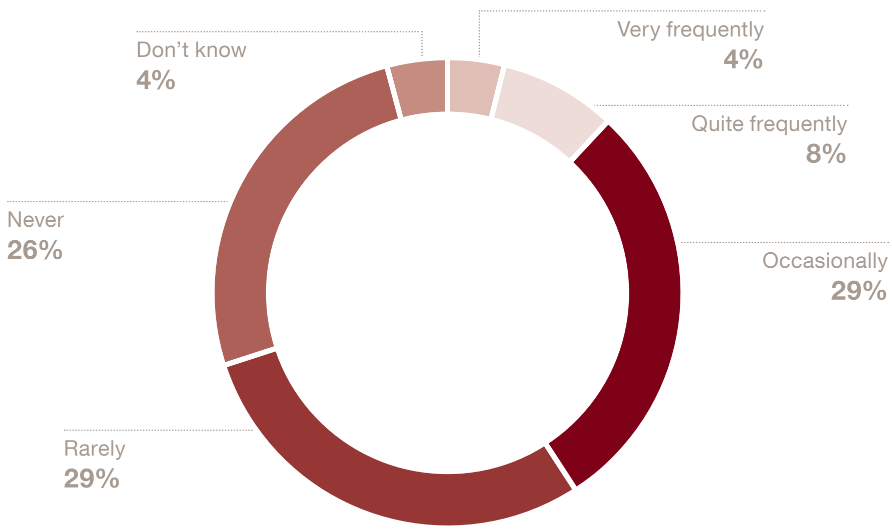
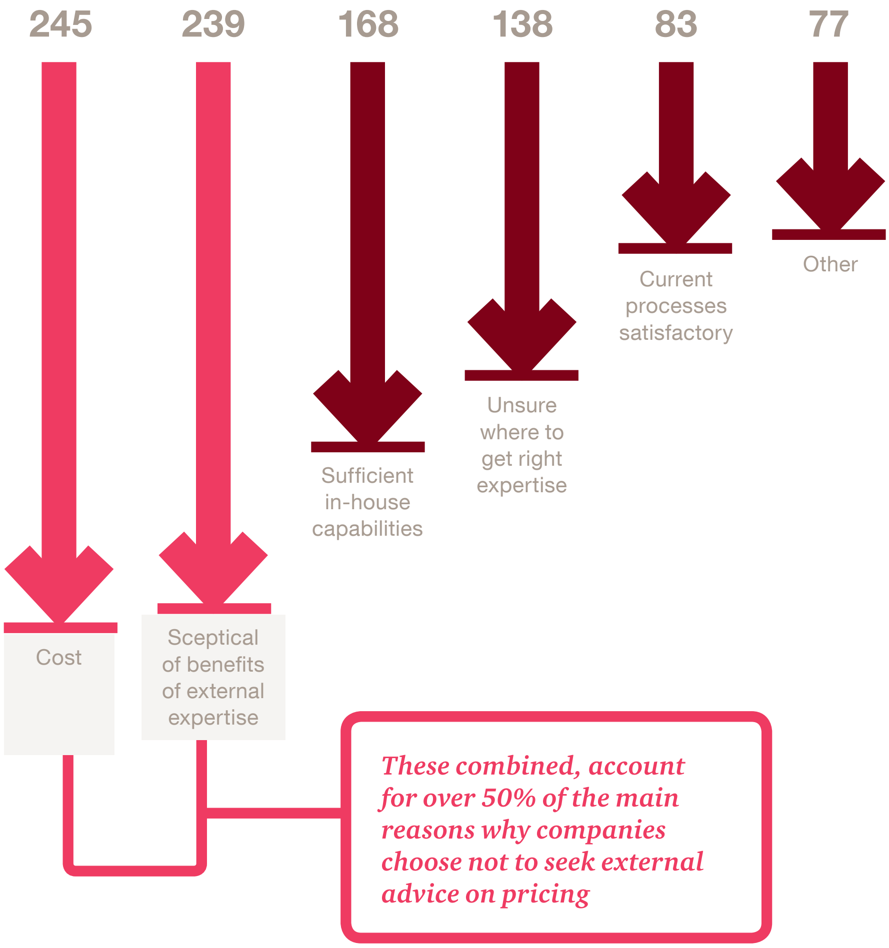


Figure 10:
Reasons given for not seeking external advice on pricing



The cost of external expertise and scepticism about the benefits account for over 50% of the main reasons for not purchasing external expertise.

There is a substantial difference between companies that are sceptical of the benefits of external advice and those that believe they have sufficient in-house capabilities.

The responses suggest that a significant proportion of companies do not believe that external advice would enable them to realise the full potential of pricing, even if they believe that the potential exists. In our experience, the benefits identified through specialist advice are almost always realised and can often outweigh the cost many times over. The results are also easily identifiable through improvements in bottom line profitability. Changing a company's pricing strategy also equips it with the tools and processes required to optimise pricing on an ongoing basis, whilst also helping to improve profit forecasting.

In summary

- The majority of respondents expect profitability improvements to be realised from structuring their pricing more effectively or improving operational effectiveness.
- Whether driven by ambition or market or competitive pressures, there is growing importance given to getting pricing right. Although around a quarter of respondents believe profits will rise over the next three years due to an increase in prices, a significant minority (17%) believe that profits will decline due to falling prices.
- Almost a third of respondents tell us they have sufficient in-house capabilities to implement such strategies. The remaining respondents, we can assume, may experience difficulties with the implementation of effective strategies.
- Over 40% of respondents seek external advice on pricing, but a quarter tell us they are unsure of where to get the right expertise from.

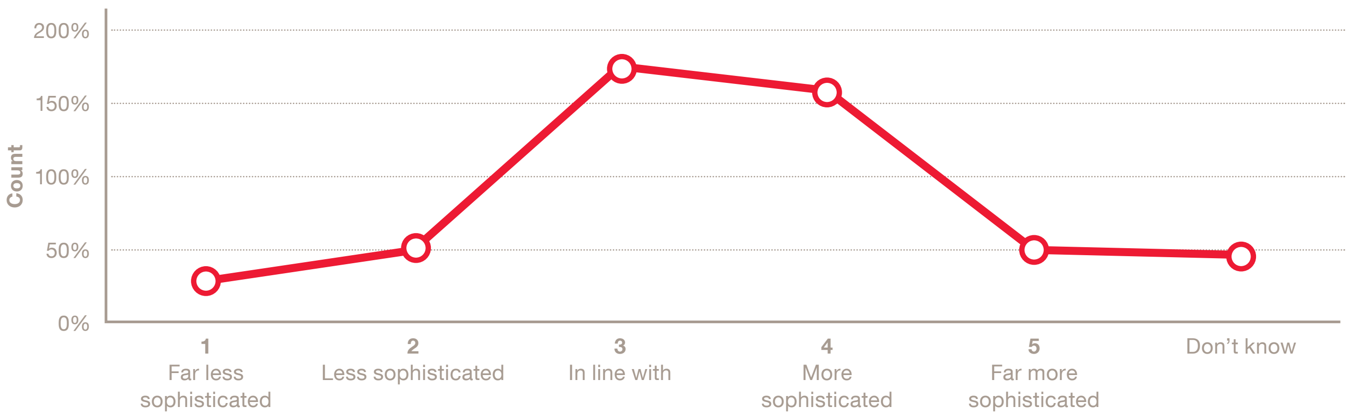
What are the leading companies doing?

The majority of respondents believe their processes are more sophisticated than their peers. However, a third say that they don't have sufficient in-house capabilities to implement effective pricing strategies.

60%

Nearly 60% of respondents said their approach to pricing includes simple methodologies of cost mark-up and/or matching competitors

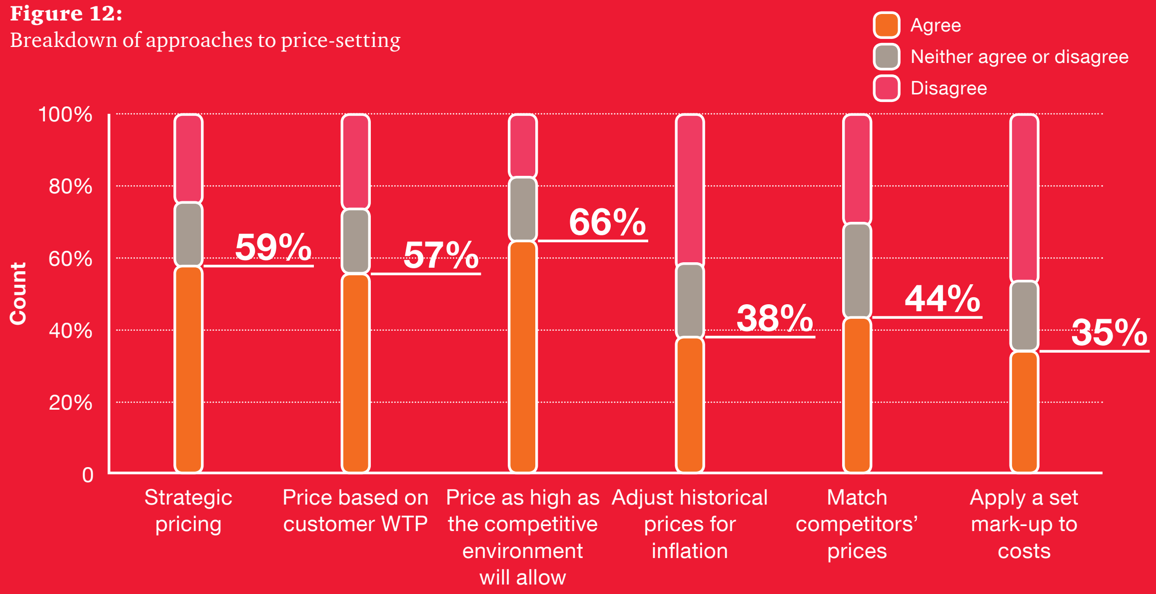
Figure 11:
Level of sophistication relative to competitors or industry peers



In fact, only 15% of respondents believe their pricing to be less sophisticated than their competitors.

To get a better picture of general pricing practices, we asked our respondents to what extent they adopt pricing strategies of differing levels of sophistication.

Figure 12:
Breakdown of approaches to price-setting



Few companies 'strongly' adopt one pricing strategy or another. Although the more unsophisticated strategies, such as a fixed mark-up to costs, appear to be less widespread, a relatively large number of respondents believe they match competitors' prices. This reactive policy is generally avoided by leading companies, preferring to price strategically, or based upon end-use value – i.e. Customer willingness to pay (WTP). But only 14% of respondents consider WTP as a primary approach to setting prices.

Case study:
Price the benefits, not the costs

In an industry where cost-plus pricing is rife, a speciality coatings manufacturer changed its pricing approach to that of pricing the benefits to the customer.

A fast-curing coating would have chemical tanks back into service 2 days faster than comparative products. The average cost to its customers of a tank being out of service was £50,000 per day. Framing it like this helped to show that the savings to the customer were significant and allowed the coatings manufacturer to increase their pricing.

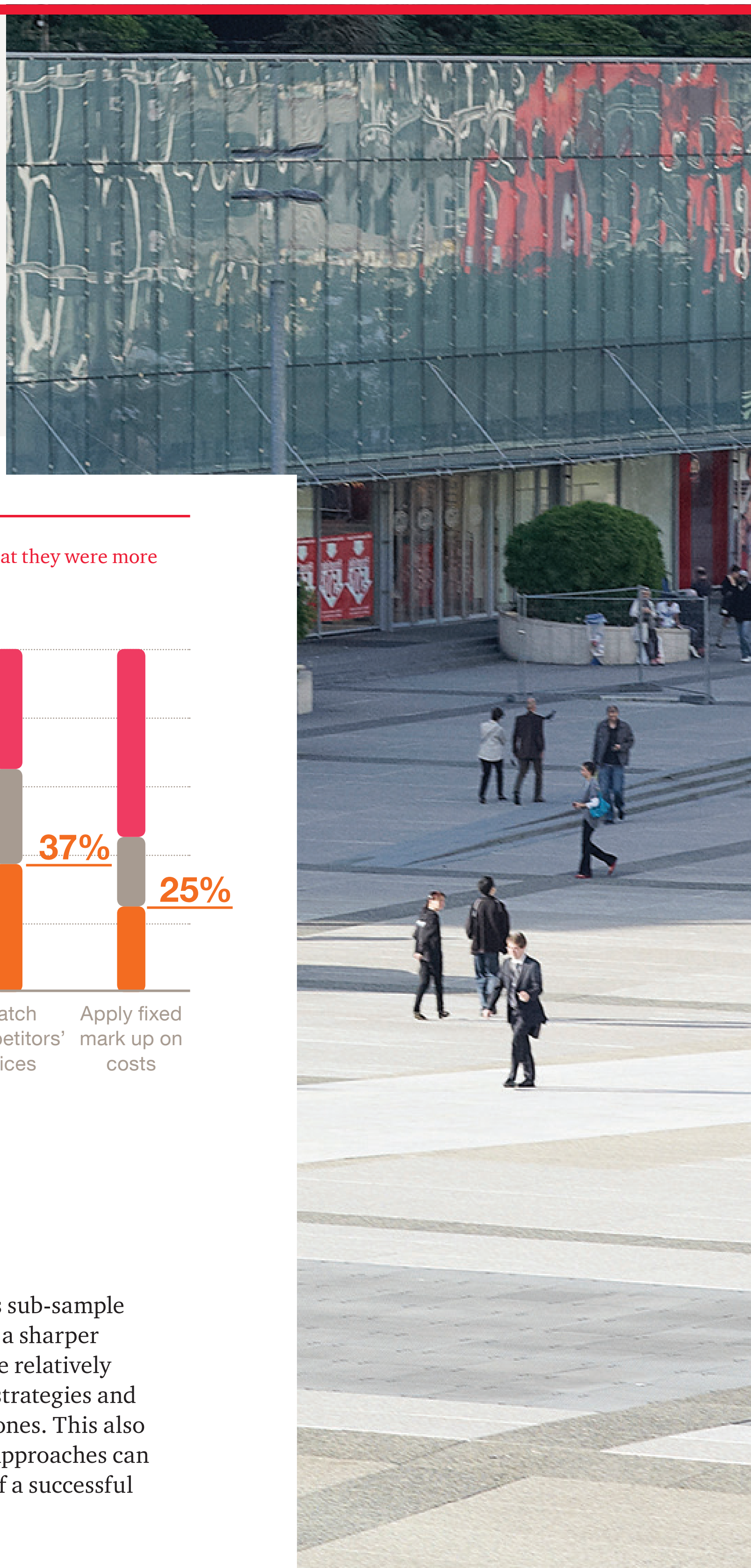
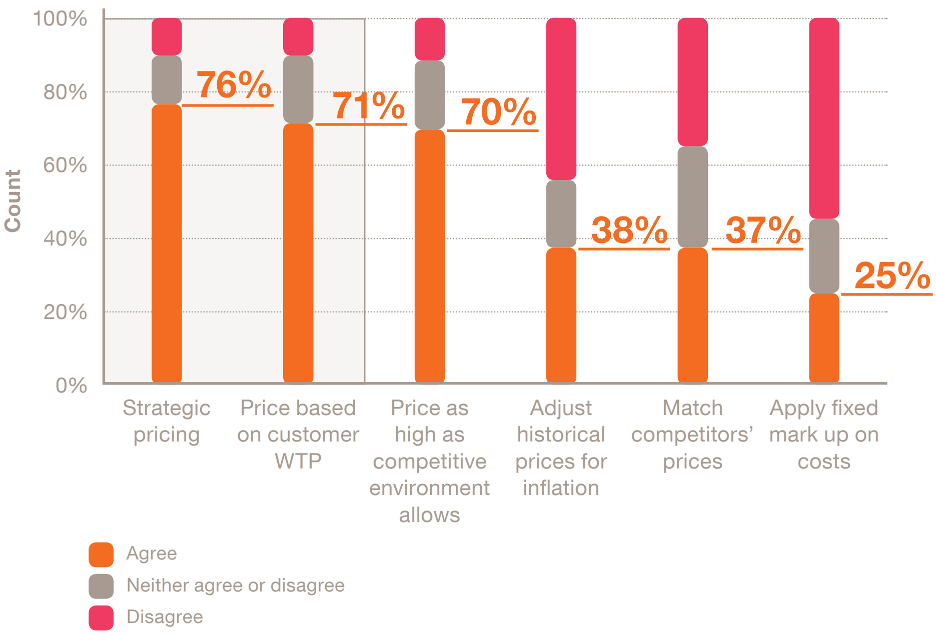


Figure 13:
Breakdown of approaches to price-setting (for respondents answering that they were more sophisticated in their approach to pricing)

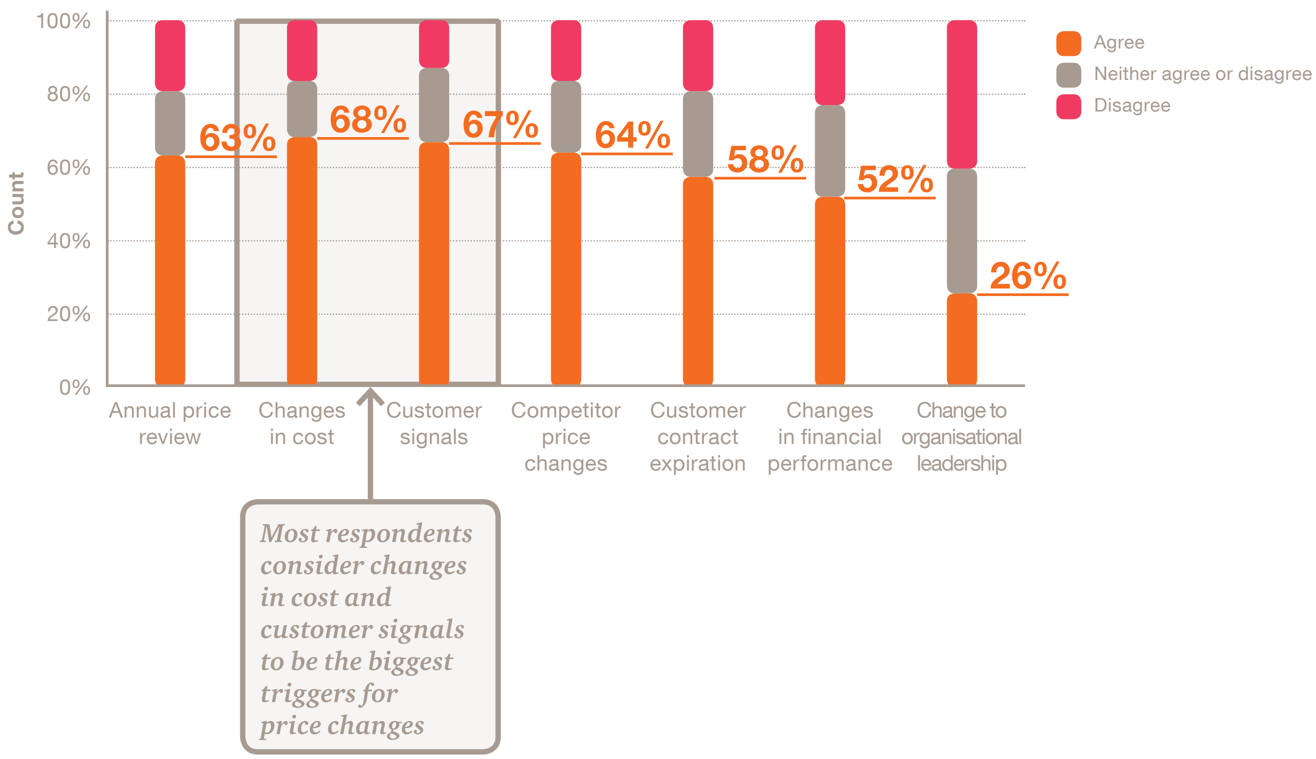


We were also interested in whether companies' own views of what constituted sophisticated pricing corresponded with our own. We have therefore looked more closely at responses from those companies stating they use 'relatively more sophisticated' pricing approaches than their competitors.

As we expected, this sub-sample of companies shows a sharper contrast between the relatively more sophisticated strategies and the more simplistic ones. This also shows that simpler approaches can still be an element of a successful pricing strategy.

We would expect the factors used to set prices to correspond to those that trigger changes. To test this, we examined the breakdown of triggers given by respondents in Figure 14 below.

Figure 14:
Breakdown of triggers for pricing changes



Case study:
When changes to costs impact on strategic pricing

An industrial products manufacturer sets prices strategically, with governance over price lists and discounts. However, its cost base is heavily reliant upon one of its key raw materials, copper. As a result, typically multi-year pricing contracts are linked to the market price of copper whereby any significant movements allow pricing reviews.

There appears to be inconsistencies in what triggers pricing changes for an organisation. For example, more companies agree that changes in costs would cause them to adjust prices than acknowledge they apply a fixed mark-up to costs. However, this may reflect other considerations; a company may be able to pass on a change in a raw material used by all its competitors, but would not apply a fixed mark-up to its own cost base without reference to competitor prices and willingness to pay.

The high proportion of companies for whom annual price reviews and contract expiration are important factors, serves to underscore the importance of better pricing.
The more infrequently that companies can, or do, make adjustments to prices, then the greater the impact will be of any pricing decisions.

<5%

Less than 5% of respondents were in the top quartile of performers for all four aspects of pricing.

Best practice across the four aspects of effective pricing

The opposite diagram shows how respondents have performed across the key ingredients to an effective pricing strategy, within the four aspects identified earlier. We have presented the average performer as well as a top quartile performer.

On average, companies are performing best across the 'Customer' aspect, possibly as a result of recent advancements in customer information capture through such methods as loyalty cards and online tracking – collecting data on customers is becoming big business.

Where companies do appear to be lagging behind is in the external looking measures, such as benchmarking competitors and tracking industry factors and forecasting. Companies are inconsistent in how effectively they apply best practice across all four aspects of pricing and very few achieve best practice in all areas.

Also shown on the diagram is one of the overall top quartile respondents. This company believes they are more sophisticated at pricing than their competitors and sees their biggest challenge in setting and executing prices as competitors lacking knowledge of the value of the product. Regardless, they expect net margins to increase over the next three years as a result of increasing prices. Unsurprisingly, this company has a pricing board who meet regularly to discuss challenges faced by the firm.

A closer examination of individual responses shows that most companies agree that they are strong in some areas and weak in others:

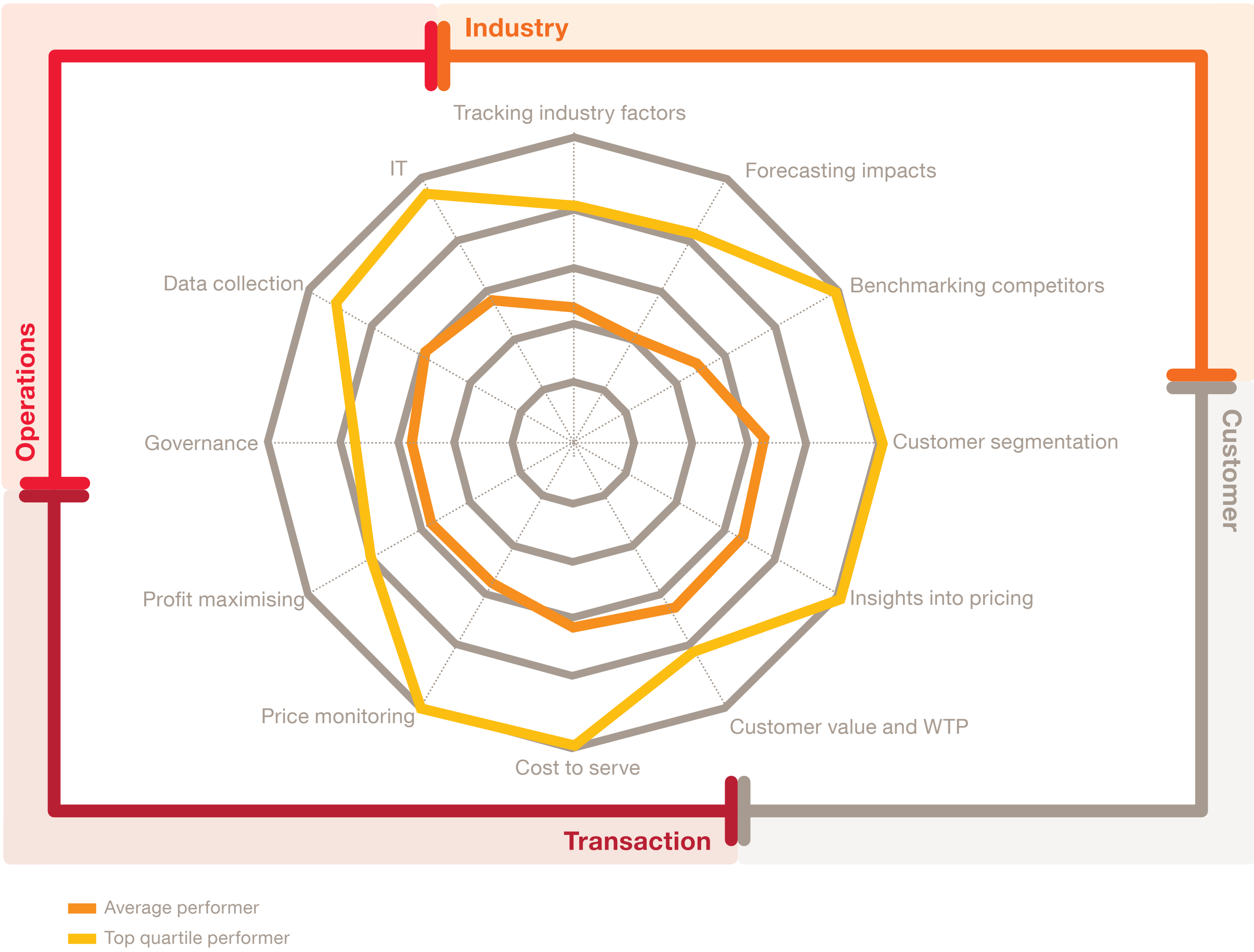
- **76%** of respondents scored in the **top quartile** for their performance in at least one of the aspects;
- but less than **5%** of respondents were in the top quartile of performers for **all** aspects;
- **19%** of companies who were in the **top quartile** of performers in at least one of the aspects also ranked in the **bottom quartile** on our or more of the others.

In an ideal world, a firm would be performing along the outer edge all the way around the diagram. You can see that, perhaps as expected, respondents on average are performing at a mid-level across almost each of the aspects.

In the next section, we present and discuss the more detailed questions we asked about how companies reflect the different factors in their pricing decisions.

4 aspects of pricing

Industry	Customer	Transaction	Operations
Tracking industry factors	Customer segmentation	Cost to serve	Governance
Forecasting impacts	Insights into pricing	Price monitoring	Data collection
Benchmarking competitors	Customer value and WTP	Profit maximising	IT



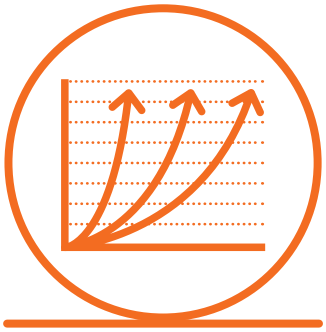
The outer edge of the spidergram represents the highest scoring performer.

The four aspects of pricing

There are many opportunities to improve pricing if you consider the four different aspects.

Optimising pricing does not always come down to simply increasing or reducing prices. Changes in product/service features, marketing strategy, channel focus or the pricing basis are often the keys to improving pricing structures. A well known example of this is low cost airlines keeping the price of luggage separate from the cost of the fare.

Looking at pricing in a structured way simplifies a complex subject and reveals opportunities for improvement. In our experience, working with companies across a range of industries, there are four aspects of pricing that are particularly useful to consider.



Industry

Industry level trends such as changes in the supply and demand, impact different industries to different degrees. However in all cases, a forward looking understanding of how an industry is changing is crucial, particularly in the current climate.

Customer

Individual customers attach differing levels of value to different product/service benefits. Deeply understanding these value associations, how customers react to price changes, and how to position offerings versus competitors, is a core competency in achieving pricing excellence.

Transaction

Understanding prices at an individual transaction level, across customers, products and channels, is critical. Knowing the true cost to serve, whether discounts are commensurate with purchase volumes and if rebates are justified, requires granular analytical insight and financial rigour.

Operations

Realising the benefits from changes in pricing requires alignment across functions, with clear responsibilities for price setting, the right organisational structure and incentives, as well as the tools, technology and processes to support pricing objectives and monitor performance.

Industry

Industry factors are often overlooked by many businesses in informing pricing strategy and making pricing decisions. Examples of industry factors include changes in the supply and demand balance, sustained input cost increases, technology disruptions, new market entrants, changes in regulation, along with many others. Understanding what the relevant factors are, and the way in which they impact your business and customers, can have a significant influence on the success of any pricing strategy.

Case study:
A manufacturing perspective

An electrical wiring manufacturer experienced a significant drop in profitability due to copper price increases and the lack of pass-through provisions in its contracts with customers. Historically this had not been an issue and the company was on the back foot in having to renegotiate terms and suffer poor trading performance which could have been largely avoided.

Case study:
A technology perspective

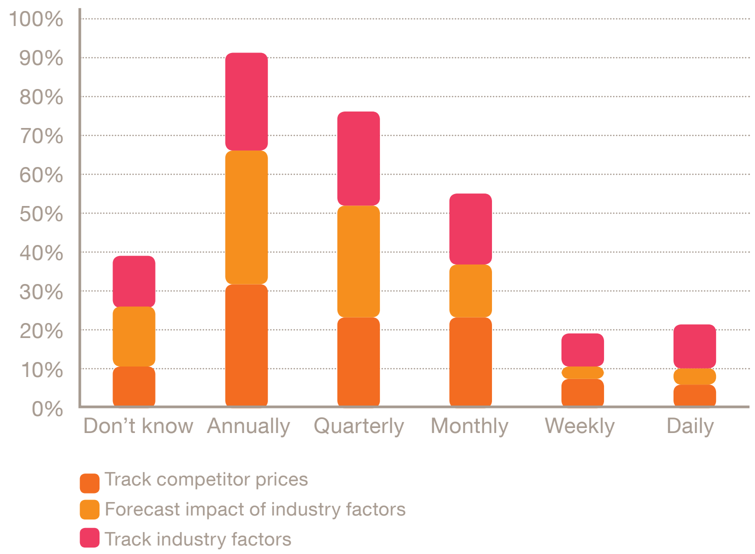
Technology buyers are increasingly looking to replace capex with opex. Software delivered through the cloud, or Software as a Service (SaaS) as it is also known, is transforming the predominant pricing model for software from a fixed licence fee model to a pay as you go model. This trend has enabled new entrants to compete with established players, many of whom have been slow to change their pricing models.

How effectively do companies track external factors?

To assess how effective companies are in applying the industry perspective to their pricing, we asked respondents whether they undertook the following analysis daily, weekly, monthly, quarterly or annually:

- Track key industry factors that influence your pricing decision (e.g. supply/demand trends, cost trends, regulatory changes)
- Forecast the impact of these industry factors on your organisation
- Track the prices of competitors, and benchmark your own prices

Figure 15:
Breakdown of how often external factors are tracked



We found that:

- Companies more often analyse historical and contemporaneous data (i.e. tracking industry factors and competitors' prices) than forward-looking data to forecast the impact on their own organisation. Although only 13% of companies tracked industry factors on a daily or weekly basis.
- Whilst differences between the major industry groups are not large, it is clear that some industries (for example retail & consumer and automotive), typically undertake all these types of analysis more frequently than others.
- Relatively small differences in averages belie potentially quite significant differences in the degree of sophistication. For example, typical industrial products companies appear to only update their forecasts quarterly, whereas for the automotive sector a significantly higher proportion of respondents do so monthly.

Customer

The deeper a business' understanding of what its customers value, the greater the opportunity to optimise pricing. The key is to ensure that customer insight is linked to pricing decisions in a systematic way.
For instance, many companies use customer segmentation to target their marketing efforts, but fail to use the insights provided by the segmentation to take advantage of pricing opportunities. This can mean that value is left on the table - an obvious example is offering discounts to customers who would have purchased at the full price anyway.

The most advanced companies, especially those operating in B2C sectors, now use behavioural insights to drive a more sophisticated understanding of customers' response to pricing and achieve the most favourable price/volume response.

This can, for example, be seen in the way that many ecommerce sites offer "free delivery" promotions, in preference to discounting the product price by an equivalent amount.

Businesses selling online have the ability to monitor customer behaviour, test what they value and to learn and improve pricing dynamically over time, at the customer segment or even individual customer level.

How well do companies know their customers?

To evaluate how well companies know their customers, we asked respondents to what extent they agreed or disagreed with a number of statements which fall into three categories:

Customer segmentation:

- "We regularly monitor how profitable our different customer segments are."
- "We segment our customers based on a detailed understanding of their needs."

Use insights to pricing:

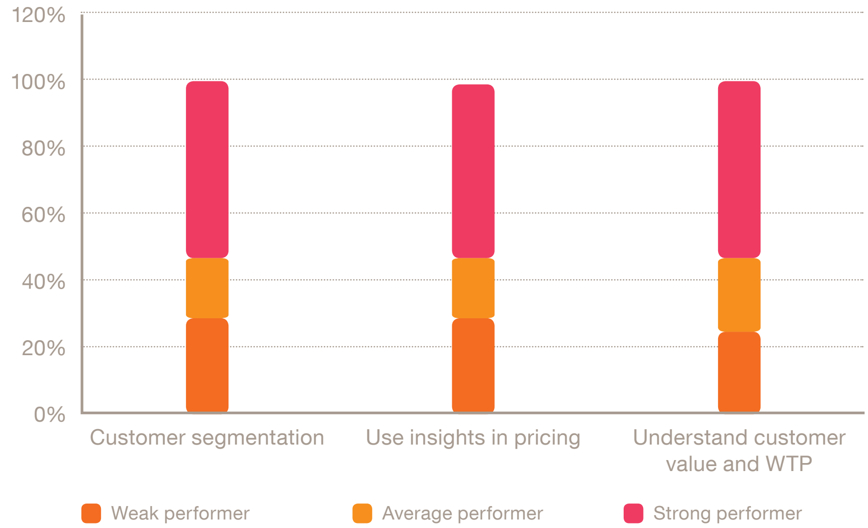
- "We use insights from our customer segmentation analysis to review our pricing decisions."
- "We understand what product / service benefits each customer segment values."

Understand customer value and willingness to pay (WTP):

- "We understand how much our customers are willing to pay for the product / service benefits."

The most commonly stated challenge in setting and executing prices is understanding customer willingness to pay

Figure 16:
Breakdown of how well companies know their customers



Note: *A small percentage of respondents who answered "Do not know" to these questions have been excluded from the figure. For this reason the percentages do not add to 100%.*

We found that whilst 50% of respondents understand what their customers value, only 13% have a deep insight into customer willingness to pay.

25% of respondents have little or no understanding of what their customers value.

> *"In the case of luxury goods, their exclusivity is a large part of their appeal, and this in turn is a function of their price, so firms usually have scope for limiting supply and charging more: Ferrari, a sportscar maker, and Mulberry, a purveyor of posh bags, have both recently signalled that they plan to do just that."*
>
> The Economist, July 2013

Transaction

If a business doesn't have the means or the inclination to analyse its performance at a transactional level, then any pricing strategy risks becoming something of a blunt instrument, neither rewarding the good nor penalising the bad.

Although something of a generalisation, the Pareto principle is typically true when looking at the structure of business profits, in that 80% of profits will be generated by 20% of customers. A business needs sufficiently granular data to understand who is contributing what in the above scenario if it is to optimise pricing and target its pricing strategies effectively.

'Costs to serve' are likely to be a significant element in defining where a customer sits in the Pareto ranking. Such costs reflect the corporate spend on 'servicing' customers (i.e. order handling, expediting and general customer support activities) and traditionally sit as overheads in the P&L account. It is not sufficient to merely understand these costs at a total level. They need to be understood at a customer level, with businesses having an understanding of how much of these services each customer is 'consuming'. This allows a 'cost to serve per customer' to be calculated, which in turn allows for effective targeted pricing strategies rather than the 'scattergun' approach which is inevitable in its absence.

Calculating costs to serve involves a typical overhead allocation exercise and usually requires a technological solution. All the major Enterprise Resource Planning (ERP) vendors have specialist applications/modules to undertake such an exercise – typically based on Activity Based Costing (ABC) principles – and there are a number of off-the-shelf packages available which can interface with transactional systems to provide similar results.

Dealing at a transactional level – being armed with costs to serve and an understanding of contributions by individual customer – is a key element of a successful pricing strategy. It allows the strands of the strategy – core prices, rebates, discounts etc. – to be mixed and matched dependant on raw data being received to deliver optimal pricing.

It undoubtedly adds an overhead in that detailed data requires additional analysis and review, but this is more than offset by the agility it provides to respond quickly and appropriately to fast changing situations which is quite simply not available to organisations operating at an aggregated level.

Do companies operate effectively at the individual transaction level?

To assess how effectively companies operate at the individual transaction level, we asked respondents about:

Cost to serve:

The extent to which they understand and measure all of the costs associated with each customer transaction or order.

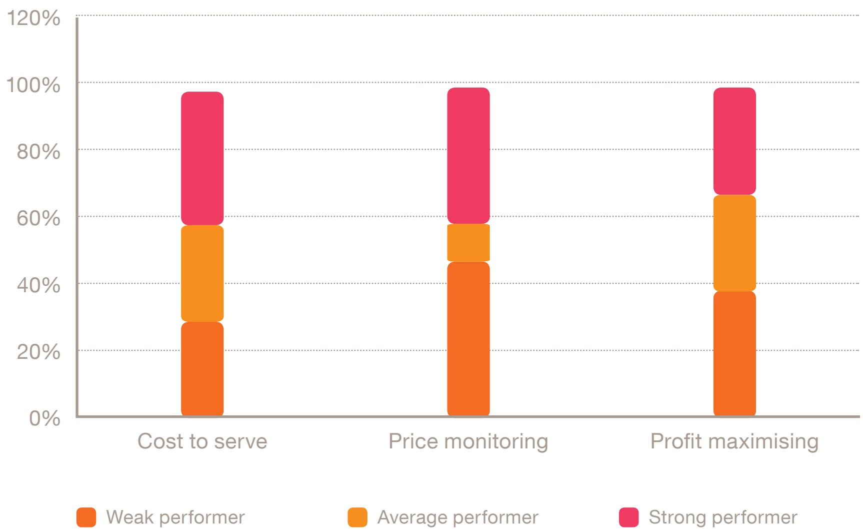
Price monitoring:

The extent to which they agree or disagree with the following statement: "We monitor each price at the transaction by transaction, order by order level".

Profit maximising:

How confident they are that prices on each customer transaction or order maximises your organisation's profitability.

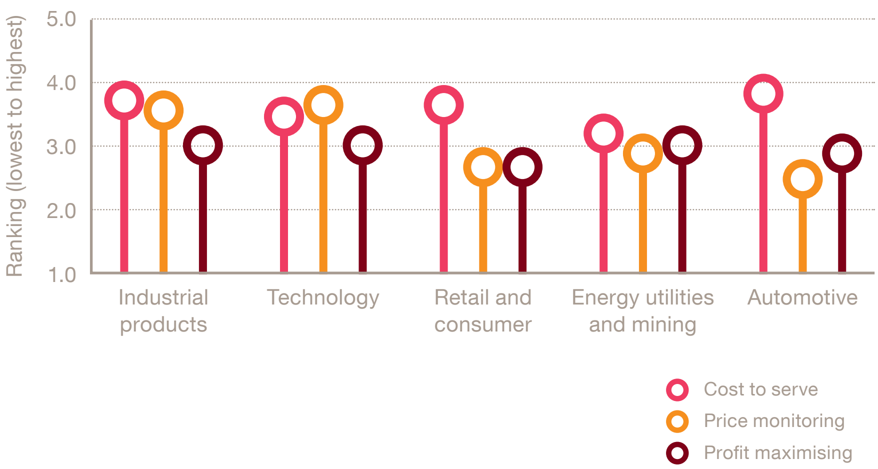
Figure 17:
Breakdown of effectiveness at individual transaction level



Note: *A small percentage of respondents who answered "Do not know" to these questions have been excluded from the figure. For this reason the percentages do not add to 100%.*

Figure 17 shows that almost 40% of companies have a good understanding of costs to serve (i.e. they are 'strong performers' in this area). A similar proportion are not confident that they set prices in a way that maximises profits (i.e. they are 'weak performers' in this area). This suggests that companies are not using the information they have to make the most of their pricing strategy.

Figure 18:
Breakdown of effectiveness at individual transaction level (by sector)



In these responses we found some larger discrepancies between sectors. For example, in industrial products, there is a greater understanding of the costs associated with each transaction, but they are no more confident that they price in order to maximise profit than, for example the automotive sector.

Operations

Companies often underestimate the importance of having clear responsibilities, alignment across people and functions, and the necessary supporting systems, when it is, in fact, core to implementing effective pricing in a number of respects.

Often, working out the right price to charge for a product or service is only part of the battle. Getting that price implemented in practice can be just as difficult. For example, in many businesses the field sales force is given some discretion to discount from list prices. In these circumstances, companies can find it difficult to make an intended price rise "stick" as increased list prices can be offset by more aggressive discounting by a sales force nervous about the impact on volumes. An effective governance structure, combined with well-designed processes can eliminate such issues.

There is an additional problem in industries where retrospective rebates, volume discounts, multiple product/service bundles or non-price incentives are prevalent. These factors can make pricing so complex that the actual end price charged to the customer can be unclear, even after the event. Regulated industries face additional issues, based on the need to have a well-documented audit trail to justify pricing levels. Capturing data, and sophisticated transactional analysis can provide some clarity, although often this is only achievable long after the event (to wait for rebates, volume bonuses etc).

Good pricing governance is key to managing issues such as these and requires clear decision rights and approval mechanisms as well as accurate and timely data.

How effective are companies' pricing governance and operations?

To assess how effective companies are in implementing, managing and monitoring prices, we asked companies about:

Pricing governance:

The extent of centralisation of price strategy and price setting; the extent of centralisation of discounting; and the analytical rigour behind the discounting approach.

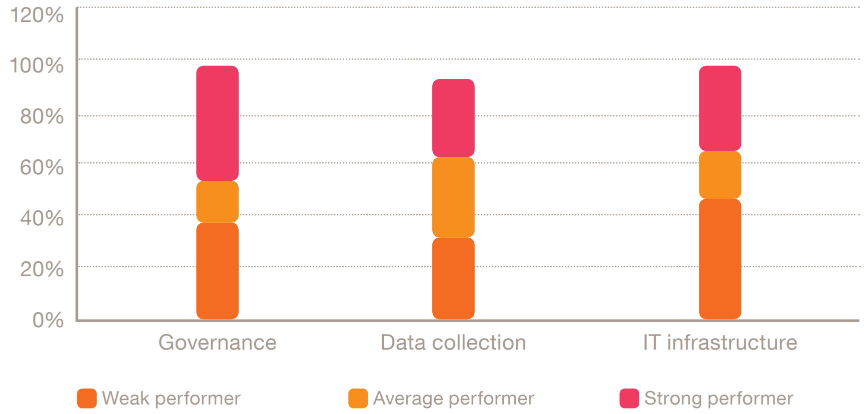
Data collection:

The frequency of customer data collection and analysis; and how they rated the quality of this data for decision-making.

IT infrastructure:

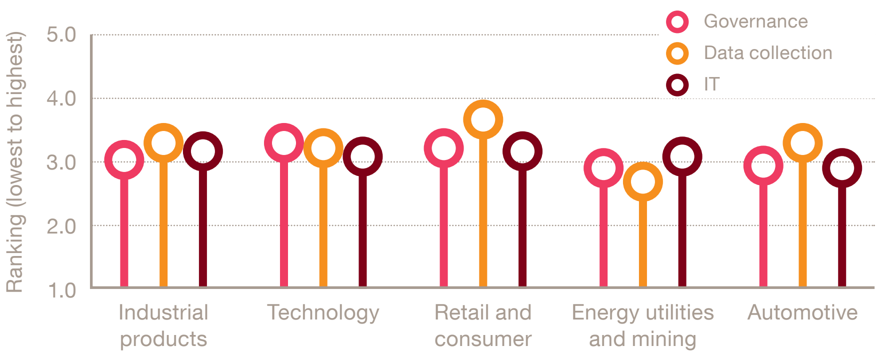
The extent to which the infrastructure integrates price setting, price optimisation and customer data; the speed with which it allows the company to process data; and whether these capabilities are actually fully exploited by the firm in its pricing.

Figure 19:
Breakdown of pricing operations



***Note:** A small percentage of respondents who answered "Do not know" to these questions have been excluded from the figure. For this reason the percentages do not add to 100%.*

Figure 20:
Breakdown of pricing operations (by sector)



The results suggest that the area where companies seem to struggle the most (47%) is in developing an IT structure which integrates price setting and does so in a way that optimises prices. A lower, but still significant proportion of respondents (37%) perform poorly when it comes to establishing a governance structure that allows centralisation of pricing strategy decisions. What is interesting is that in both these areas (IT infrastructure and governance), there are not many average performers, suggesting that most companies either have made an effort or not at all.

There is a fairly even spread in how companies perform in collecting and analysing data.

Looking at the data by sector shows that retail and consumer perform the highest as they most frequently collect and analyse data. On the other hand, energy utilities and mining perform lowest in this area.

Conclusions and key takeaways

In a world in which investors are more demanding, customers more fickle and competitors fight aggressively for market share, pricing is one of the biggest levers you can pull to make an impact on your bottom line.

In many cases, it's a more attractive option than others, with mergers and acquisitions or partnerships difficult to structure when capital is constrained and cost reduction and financial restructuring programmes require major and potentially expensive change.

It is clear from our survey results that the majority of companies already recognise the potential to achieve growth through improved pricing.

What's interesting is that most companies recognise that understanding their customers and being able to react to customers is often what drives pricing, yet in reality a very small proportion (13%) have an in depth understanding of what their customers value and what they're willing to pay. This may be because using customer values is arguably one of the more complex ways of setting prices and companies are often nervous about changing prices in a way that could have a negative impact on customer behaviour. It is perhaps for this reason that we see that 60% of respondents use simpler methodologies such as cost mark-up or matching competitors.

Implementing a great pricing strategy can be complex and involves excellence in all four aspects. But when taken seriously, with a clear strategy in place, pricing can help make your company more profitable now and in the future.

Want to find out more?

If you're looking to make an immediate impact on your bottom line through more effective pricing, please contact one of our team below, or visit our website *http://www.pwc.co.uk/consulting/pricing*. Whatever the scenario, we use a simple framework which considers pricing from different perspectives and unearths opportunities for improvement.

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How we can help

There are four distinguishing elements of our framework:

- Specialist techniques and insights – such as willingness to pay analysis, elasticity modelling, behavioural economics and scenario modelling– that can provide a rich picture of the pricing level, structure and dynamics of your organisation.
- A tool we've developed called Equazion, which uses company information to build a picture of product and customer profitability in order to identify areas for improvement. Equazion can also form part of a sustainable implementation.
- Operational insights from our practical experience of what often gets in the way of translating pricing strategy into practice.
- Supporting and coaching in the implementation of pricing, including the introduction of pricing software.

Appendix: Home countries of respondents

1. Albania
2. Argentina
3. Australia
4. Belgium
5. Brazil
6. Canada
7. China
8. Colombia
9. Czech Republic
10. Denmark
11. DR Congo
12. France
13. Germany
14. Greece
15. Honduras
16. Hungary
17. India
18. Indonesia
19. Ireland
20. Italy
21. Lithuania
22. Mexico
23. Netherlands
24. New Zealand
25. Norway
26. Other (all)
27. Pakistan
28. Panama
29. Peru
30. Poland
31. Portugal
32. Romania
33. Russia
34. Singapore
35. South Africa
36. Spain
37. Sweden
38. Switzerland
39. Thailand
40. UAE
41. UK
42. USA

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